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SMU Law Review

Volume 68 | Issue 2

Article 7

2015

The Fight over Home Court: An Analysis of the SEC's Increased Use of Administrative Proceedings

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THE FIGHT OVER HOME COURT: AN ANALYSIS OF THE SEC'S INCREASED USE OF ADMINISTRATIVE PROCEEDINGS

*Ryan Jones**

TABLE OF CONTENTS

I. INTRODUCTION	508
II. A BRIEF HISTORY OF SEC ADMINISTRATIVE PROCEEDINGS	510
A. THE SECURITIES AND ENFORCEMENT REMEDIES AND PENNY STOCK REFORM ACT OF 1990.....	511
B. THE 1993 AND 1995 REVISIONS TO THE SEC'S RULES OF PRACTICE	513
C. THE SARBANES-OXLEY ACT	514
III. THE CURRENT STATE OF SEC ADMINISTRATIVE ENFORCEMENT	515
A. THE DODD-FRANK ACT.....	516
B. A STATISTICAL OVERVIEW OF SEC ADMINISTRATIVE PROCEEDINGS, POST-DODD-FRANK	517
IV. AN ANALYSIS OF SEC ADMINISTRATIVE ENFORCEMENT, POST-DODD-FRANK	519
A. DISTRICT COURT STANDING FOR CONSTITUTIONAL CHALLENGES	520
B. DUE PROCESS AND EQUAL PROTECTION ISSUES	523
1. <i>Due Process Challenges and Procedural</i> <i>Disadvantages</i>	523
a. ALJ Decision Deadlines	524
b. Discovery Limitations	525
c. Absence of a Right to Trial by Jury	525
d. Looser Evidentiary Standards	526
2. <i>Equal protection claims</i>	527
3. <i>Chevron deference</i>	527
C. APPOINTMENTS CLAUSE ISSUES.....	528
1. <i>Analyzing Free Enterprise Fund v. PCAOB</i>	528
2. <i>Applying Free Enterprise Fund v. PCAOB</i>	529

* J.D. Candidate, SMU Dedman School of Law, May 2016; B.S.M., Tulane University, May 2013. I would like to thank Professor Marc Steinberg for his helpful comments and edits on a prior draft. I would also like to thank my father and mother, Scott Jones and Susan Jones, for their endless, unconditional love and support.

a.	Are SEC Administrative Law Judges Officers?	529
b.	Are the ALJs Separated from Presidential Removal by Two or More Layers of For-Cause Protection?	530
c.	Do the ALJs Exercise Substantial Executive Authority?	531
D.	INCREASED EMPHASIS ON "WINNING" AND COLLECTING MONETARY PENALTIES	532
E.	OTHER EXTERNAL INDICATORS OF BIAS	532
V.	A PROPOSAL TO REFORM THE SEC ADMINISTRATIVE ENFORCEMENT PROCESS	533
A.	DEVELOP OBJECTIVE CRITERIA FOR BRINGING ADMINISTRATIVE PROCEEDINGS	534
B.	REVISE THE SEC RULES OF PRACTICE	535
VI.	CONCLUSION	536

ABSTRACT

The Dodd-Frank Act of 2010 gave the SEC new authority to pursue monetary penalties through its in-house administrative court system, rather than in federal court. Since then, the Commission has won the overwhelming majority of these administrative proceedings, over which one of five SEC-appointed judges preside, including 219 successive favorable decisions from October 2013 to January 2015. Doubling down, the Commission has begun bringing more complaints in its administrative court than ever before, fully leveraging the procedural advantages the in-house system has over federal court, including no right to trial by jury, looser evidentiary standards, and a dramatically shortened discovery period.

This Article argues that the Commission's lack of regulating guidelines for its administrative proceedings deprives litigants of due process. Additionally, this Article shows that a strict reading of Supreme Court precedent dictates that executive control over the Commission's administrative law judges is too attenuated under the Appointments Clause. To solve this problem, this Article proposes that Congress or the SEC institute objective criteria for bringing administrative proceedings and revise the SEC's Rules of Practice.

I. INTRODUCTION

THE U.S. Securities and Exchange Commission (SEC) employs a variety of legal mechanisms to enforce federal securities law,¹ but in the last five years, the SEC has increasingly utilized one particular mechanism: enforcement proceedings brought within its internal court

1. See James D. Cox & Randall S. Thomas, *SEC Enforcement Heuristics: An Empirical Inquiry*, 53 DUKE L.J. 737, 746-49 (2003).

system, similar to those used by many administrative agencies.² This system differs from the federal court system and favors the Commission in several significant ways.³ For instance, one of five SEC-appointed administrative law judges (ALJs), rather than federally appointed Article III judges, preside over the proceedings.⁴ Respondents cannot receive trial by jury.⁵ The mandated discovery period is greatly expedited in comparison to the federally mandated discovery period.⁶ Additionally, the ALJ must issue his decision within 300 days of the proceeding's start, even in the most complex securities law cases.⁷

Respondents have felt the effects of this increased use in full force. In fiscal year 2014, the SEC instituted 610 administrative proceedings—more than twice as many as in 2005, when it instituted 294.⁸ The SEC's most recent, formidable winning streak spans more than 219 administrative decisions from October 2013 to January 2015.⁹ In September 2014, the Commission began adding complex insider trading cases to its internal court system's docket,¹⁰ and administrative proceedings now make up more than 80% percent of the SEC's total caseload.¹¹ These statistics, along with the inherent makeup of the in-house court system, have led some legal experts to conclude these proceedings suffer from “potential bias,” harming respondents who might have received a fairer trial in federal court.¹²

This Article analyzes the SEC's recent increased use of administrative proceedings, constitutional attacks to such use, and proposed procedural reforms. Because these proceedings deprive respondents of significant due process and procedural protections in increasingly complex securities cases, this Article concludes that the SEC is abusing its discretion to try cases through its internal court system in lieu of federal district courts. Respondents have recently responded to this abuse by levying constitutional challenges in federal court to the entire SEC in-house court system, primarily on Due Process and Appointments Clause grounds.¹³ Many of the cases are still in district court and several have been dismissed or

2. See Jean Eaglesham, *SEC Steers More Trials to Judges It Appoints*, WALL ST. J., Oct. 21, 2014, at A1.

3. See Peter J. Henning, *The S.E.C.'s Use of the 'Rocket Docket' is Challenged*, N.Y. TIMES DEALBOOK (Aug. 25, 2014, 11:48 AM), http://dealbook.nytimes.com/2014/08/25/the-s-e-c-s-use-of-the-rocket-docket-is-challenged/?_r=0.

4. See *id.*

5. See *id.*

6. See *id.*

7. See Gretchen Morgenson, *At the S.E.C., A Question of Home-Court Edge*, N.Y. TIMES, Oct. 6, 2013, at B1.

8. See *infra* Figure 1.

9. *Id.*

10. *Id.*

11. See *id.*

12. Morgenson, *supra* note 7.

13. See Peter J. Henning, *S.E.C. Faces Challenges Over the Constitutionality of Some of its Court Proceedings*, N.Y. TIMES DEALBOOK (Jan. 27, 2015), <http://dealbook.nytimes.com/2015/01/27/s-e-c-faces-challenges-over-the-constitutionality-of-some-of-its-court-proceedings/>.

settled.¹⁴ But given the amount of respondents persistently filing such challenges and the implications of these arguments for other administrative agencies, the circuit courts—and perhaps, eventually, the Supreme Court—will probably review these cases in the near future. These courts should ignore the instinct to protect the administrative status quo and rule in favor of the administrative respondents’ constitutional challenges.

But even if these constitutional attacks are successful, many of the underlying procedural problems with this administrative court system will likely remain. Only the SEC commissioners or Congress can resolve these problems, instituting guidelines for bringing administrative proceedings and installing procedural protections more similar to those afforded in federal court. The SEC-appointed judges would remain, of course, but the protections would appropriately reflect the increasingly complex nature of the cases that the Commission brings in-house.

Part II of this Article explores the history of the SEC’s administrative proceedings as an enforcement mechanism and explains how several reforms over the last three decades have granted the Commission a greater “home court advantage.” Part III discusses how the Dodd-Frank Act of 2010 prompted the SEC’s increased use of these proceedings, especially in complex-litigation cases against entities that the SEC does not directly regulate. Part IV discusses how this increased use has unfairly affected administrative respondents and analyzes the merits of constitutional attacks that these respondents have raised in the district courts. Finally, Part V proposes procedural reforms to the SEC’s current in-house court system.

II. A BRIEF HISTORY OF SEC ADMINISTRATIVE PROCEEDINGS

Congress created the SEC in 1934¹⁵ to serve the public.¹⁶ The agency’s purpose, generally, “was to prevent fraud and create full disclosure to allow investors to make informed decisions.”¹⁷ The SEC fulfills this purpose in many different ways, one of which is disciplinary action “performed by the Commission under the various federal securities statutes.”¹⁸ It “consists of five Commissioners, appointed by the Presi-

14. *See id.*

15. Securities Exchange Act of 1934, Pub. L. No. 73-291, 48 Stat. 881 (codified as amended at 15 U.S.C. §§ 78a–78pp (2006 & Supp. V 2011)). *See generally* 1 LOUIS LOSS, JOEL SELIGMAN & TROY PAREDES, FUNDAMENTALS OF SECURITIES REGULATION 57–60 (6th ed. 2011) (providing an overview of the Acts).

16. *See S.E.C. v. Mgmt. Dynamics, Inc.*, 515 F.2d 801, 808 (2d Cir. 1975) (noting the SEC is a “statutory guardian charged with safeguarding the public interest in enforcing the securities laws”); *see also* Matthew P. Wynne, Note, *Rule 10b-5(b) Enforcement Actions in Light of Janus: Making the Case for Agency Deference*, 81 FORDHAM L. REV. 2111, 2116–17 (2013).

17. Wynne, *supra* note 16, at 2116.

18. 25 MARC I. STEINBERG AND RALPH C. FERRARA, SECURITIES PRACTICE FEDERAL & STATE ENFORCEMENT § 4:1 (last updated Sept. 2014); *see also* 15 U.S.C. § 78j(b) (making it unlawful to act “in contravention of such rules and regulations as the Commission

dent, who collectively oversee five separate divisions, including a Division of Enforcement.”¹⁹ With nearly 1,300 employees, the Division of Enforcement is the SEC’s largest division,²⁰ having grown by nearly 60% over the past twenty-three years.²¹ It has three primary objectives: “protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation.”²²

With few exceptions, the SEC’s Division of Enforcement brings securities enforcement actions either in a district court proceeding or in an administrative proceeding,²³ over which an administrative law judge presides.²⁴ The Division of Enforcement “is a party to the action and must prove its case.”²⁵ After the ALJ renders a decision, it may be appealed to the five-person Commission.²⁶ The Commission’s decision may then be “appealed by an aggrieved respondent to an appropriate federal appellate court.”²⁷ The following subsections explain how the SEC’s powers within administrative proceedings expanded over the two decades leading up to the passage of the Dodd-Frank Act.

A. THE SECURITIES AND ENFORCEMENT REMEDIES AND PENNY STOCK REFORM ACT OF 1990

During the 1980s, the SEC’s enforcement actions began to “shift from remedial to punitive in nature,” and through the Insider Trading Sanctions Act of 1984²⁸ and the Insider Trading and Securities Fraud Enforcement Act of 1988,²⁹ the Commission received greater power to penalize insider trading and other select securities law violations.³⁰ In its proposal

may prescribe as necessary or appropriate in the public interest or for the protection of investors”).

19. Wynne, *supra* note 16, at 2118 (citing *About the SEC: What We Do*, SEC, available at <http://www.sec.gov/about/whatwedo.shtml> (last visited Feb. 15, 2013)).

20. Michael S. Piwowar, Comm’r, U.S. Sec. & Exch. Comm’n, Remarks to the Securities Enforcement Forum 2014 (Oct. 14, 2014) (transcript available at http://www.sec.gov/News/Speech/Detail/Speech/1370543156675#_ftnref20).

21. Paul S. Atkins & Bradley J. Bondi, *Evaluating The Mission: A Critical Review Of The History And Evolution Of The SEC Enforcement Program*, 13 FORDHAM J. CORP. & FIN. L. 367, 371, n.10 (2008).

22. U.S. SEC. & EXCH. COMM’N, 2006 PERFORMANCE AND ACCOUNTABILITY REPORT 5, available at <http://www.sec.gov/about/secpar/secpar2006.pdf> (last visited Jan. 26, 2015).

23. The procedures governing such proceedings are found principally in the Administrative Procedure Act, 5 U.S.C.A. §§ 551 et seq. (2012), and in the Commission’s Rules of Practice, 17 C.F.R. § 201 (2015).

24. Atkins & Bondi, *supra* note 21, at 372.

25. STEINBERG & FERRARA, *supra* note 18, § 4:42 (last updated Sept. 2014) (citing Theodore A. Levine, Ralph C. Ferrara & James J. Moylan, *Administrative Proceedings Under the Securities Exchange Act of 1934*, 25 MERCER L. REV. 671, 674–85 (1974)).

26. See 17 C.F.R. § 201.110 (2015).

27. See 15 U.S.C. § 78y(a)(1) (2006 & Supp. V 2011); see also 15 U.S.C. § 77i. (2006 & Supp. V 2011); STEINBERG & FERRARA, *supra* note 18, § 4:42 (last updated Sept. 2014) (citing Section 25 of the Exchange Act, 15 U.S.C. § 77i (2012)).

28. Insider Trading Sanctions Act of 1984, Pub. L. No. 98-376, § 1, 98 Stat. 1264 (1984) (codified as amended in scattered sections of 15 U.S.C.).

29. Insider Trading and Securities Fraud Enforcement Act of 1988, Pub. L. No. 100-704, § 1, 102 Stat. 4677 (1988) (codified as amended in scattered sections of 15 U.S.C.).

30. See Atkins & Bondi, *supra* note 21, at 383–85.

for a third expansion of enforcement authority, much of which became the Securities and Enforcement Remedies and Penny Stock Reform Act of 1990 (“Reform Act”),³¹ the SEC sought and eventually received the power to (1) impose monetary penalties in administrative proceedings involving violations of securities law against entities directly regulated by the SEC; (2) issue temporary and permanent cease-and-desist orders against regulated and non-regulated entities; and (3) “seek orders from federal district courts prohibiting persons who violate certain antifraud provisions from serving as officers and directors of reporting companies upon a showing of substantial unfitness.”³²

Just as significant, however, is what the SEC sought in its first Reform Act proposal that it did not receive: the power to seek or impose monetary penalties in administrative proceedings against entities that the Commission did not directly regulate.³³ When the SEC initially offered its recommendations for the legislation, it advocated for the inclusion of such power and separately proposed guidelines that it would use to determine when to seek monetary penalties.³⁴ The agency stressed that it would not pursue such penalties in every administrative proceeding and “explained that penalties should be assessed against [non-regulated entities] only in the rare situation where the [entity] received a ‘direct economic benefit’ from the fraud.”³⁵ Even in those circumstances, the Commission said, it would refrain from seeking penalties if “the passage of time and resulting shareholder turnover” weighed against their imposition.³⁶ True to the SEC’s primary goal since its creation,³⁷ the Commission would always analyze whether seeking penalties was “in the public interest,” along with at least six other factors.³⁸

But consistent with Congress’s wishes, the SEC modified its recommendations in the succeeding months, removing its request for power to pursue monetary penalties against non-regulated entities in administrative proceedings.³⁹ Under the revised legislative framework, the Commission could still seek such penalties “but only in federal court proceedings.”⁴⁰ This revised proposal eventually became the Reform Act.⁴¹ These revisions make clear that Congress wanted to ensure that a judicial check—independent of the SEC’s in-house court system—existed to constrain the Commission’s monetary penalty-seeking power:

31. Securities Enforcement Remedies and Penny Stock Reform Act of 1990, Pub. L. No. 101-429, 104 Stat. 931 (1990).

32. STEINBERG & FERRARA, *supra* note 18, § 6:1 (last updated Sept. 2014).

33. See Atkins & Bondi, *supra* note 21, at 389–94.

34. *Id.* at 389–90.

35. *Id.* at 390.

36. *Id.*

37. See Wynne, *supra* note 16, at 2116–17.

38. See Atkins & Bondi, *supra* note 21, at 391.

39. *Id.* at 392.

40. *Id.* at 393.

41. *Id.* at 392.

The concern among members of Congress and internally at the SEC was that if the same remedies were available to the SEC under both judicial and administrative proceedings, then the SEC might be perceived to have an incentive to conduct more enforcement actions through its own administrative proceedings, rather than before a federal district court judge. The final legislation did not include penalty authority in administrative proceedings precisely because there would be no oversight by Article III judges as there would be in civil proceedings.⁴²

As a result of these procedural safeguards and the SEC's general enforcement philosophy, the Commission brought only four actions monetary penalties cases against non-regulated entities between 1990 and 2002, and the amount of penalties sought totaled less than \$5 million.⁴³

B. THE 1993 AND 1995 REVISIONS TO THE SEC'S RULES OF PRACTICE

The Reform Act greatly increased the SEC's administrative power, but its own procedural Rules of Practice proved a separate obstacle to exercising that power.⁴⁴ The amount of administrative proceedings increased throughout the 1980s and, as a result, the amount of appeals from those proceedings to the Commission increased.⁴⁵ The SEC subsequently organized a Task Force on Administrative Proceedings to "identify sources of delay in those proceedings and to recommend steps to make the adjudicatory process more efficient and effective."⁴⁶ The Task Force issued a 1993 report finding that, between 1982 and 1990, the time the Commission took to finish appeals from ALJ decisions had increased by 75%.⁴⁷ Further, the Commission issued only 22 decisions in 1990, though that number had begun to increase steadily by 1993.⁴⁸

The Task Force, therefore, recommended revisions to the Rules of Practice that governed its administrative proceedings in order to increase the proceedings' efficiency.⁴⁹ These revisions, along with further revisions made in 1995, introduced many of the procedural devices that respondents bemoan today, the most significant of which were the Guidelines for the Timely Completion of Proceedings.⁵⁰ Among other things, these revisions provided for streamlined discovery process, authorized ALJs to issue subpoenas calling for the production of documents at the prehearing stage, and allowed ALJs ten months from the issuance of order for

42. *Id.* at 393–94.

43. *Id.* at 394.

44. See STEINBERG & FERRARA, *supra* note 18, § 4:1.

45. *Id.*

46. Rules of Practice, Exchange Act Release No. 33,163, 55 SEC Docket 1001 (Nov. 5, 1993).

47. See STEINBERG & FERRARA, *supra* note 18, § 4:1.

48. *Id.*

49. Rules of Practice, Exchange Act Release No. 33,163, 55 SEC Docket 1001 (Nov. 5, 1993).

50. *Id.*

administrative proceedings to issue a decision.⁵¹ However, the new adjudication deadlines are not inflexible, especially in complex matters, and can be extended “for good cause.”⁵² Further, the SEC said that the guidelines would “need to be examined periodically and may need to be readjusted in light of changes in the Commission’s case load and the availability of Commission resources.”⁵³ The SEC again revised its Rules of Practice in 2003, and it further shortened ALJ and Commission decision-issuance deadlines, along with certain brief-filing deadlines.⁵⁴

C. THE SARBANES-OXLEY ACT

Enacted in July 2002 after several prominent corporate scandals,⁵⁵ the Sarbanes-Oxley Act represented another significant expansion of the SEC’s enforcement authority.⁵⁶ Beginning with the 1990 Reform Act, the Commission could deprive securities law violators of ill-gotten gains through “disgorgement” in an administrative proceeding.⁵⁷ This enforcement mechanism is not considered a monetary penalty but rather an equitable remedy.⁵⁸ After the Reform Act’s passage, the Commission typically made disgorged funds available “for restitution and other relief for those harmed by [a] defendant’s misconduct.”⁵⁹ Section 308(a) of Sarbanes-Oxley took that concept one step further by adding monetary penalties to a “Fair Fund” for restitution and relief, provided that disgorgement had also occurred.⁶⁰ Thus, the SEC could not make the monetary penalties available when disgorgement had not taken place, despite the fact that the Commission had requested such authority.⁶¹

About one year after Sarbanes-Oxley’s passage, the SEC proposed amendments to the act that would grant the Commission power to add monetary penalties to Fair Funds even when no disgorgement occurred.⁶² The amendments, however, never passed Congress because of a “general

51. *Id.*

52. *Id.*

53. *Id.*

54. Securities Act Release No. 8240, Exchange Act Release No. 2137, Investment Company Act Release No. 34-48,018, 80 SEC Docket 1266 (June 11, 2003); 68 Fed. Reg. 35787 (July 17, 2003).

55. See Atkins & Bondi, *supra* note 21, at 394–95.

56. Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (2002) (codified in scattered sections of 11, 15, 18, 28, and 29 U.S.C.).

57. See Securities Enforcement Remedies and Penny Stock Reform Act of 1990, Pub. L. No. 101-429, 104 Stat. 931 (1990) (codified as amended at 15 U.S.C. § 78u-3(e) (2000)).

58. See Atkins & Bondi, *supra* note 21, at 386.

59. See Cox & Thomas, *supra* note 1, at 753–54.

60. Sarbanes-Oxley Act of 2002, 15 U.S.C. § 7246(a) (2012).

61. *It’s only FAIR: Returning Money to Defrauded Investors: Hearing Before the H. Subcomm. on Capital Mkts., Ins., & Gov’t Sponsored Enters. of the H. Comm. on Fin. Servs.*, 108th Cong. 5 (2003) (statement of Stephen Cutler, Director of Enforcement, U.S. Sec. & Exch. Comm’n).

62. See Press Release, Congressman Richard Baker, Oxley Introduce Bill To Strengthen SEC Powers Against Securities Fraud, Return Funds To Defrauded Investors (May 21, 2003), available at http://web.archive.org/web/20030602192406/www.baker.house.gov/News/fair_bill.htm.

unwillingness” to revisit Sarbanes-Oxley.⁶³ Of course, such power would have only given the SEC further motivation to seek monetary penalties as a quasi-equitable remedy, though such penalties are actually punitive and more speculative in nature.⁶⁴

Section 308(a) had the obvious upside of making more money available to victims of securities law violations.⁶⁵ Of course, it provided even further incentive to use administrative proceedings for seeking monetary penalties against entities that the SEC directly regulated.⁶⁶ Therefore, one primary disincentive to bringing administrative proceedings against non-regulated entities remained: the SEC could still only seek monetary penalties through a district court proceeding.⁶⁷

III. THE CURRENT STATE OF SEC ADMINISTRATIVE ENFORCEMENT

After Sarbanes-Oxley’s passage, the SEC made full use of the Fair Fund provision,⁶⁸ pursuing large monetary penalties through settlement as well as administrative and federal court proceedings more aggressively than at any other point in the Commission’s existence.⁶⁹ The SEC immediately levied its first \$10 million monetary penalty against a public company in its 2002 settlement with Xerox.⁷⁰ In 2004, it collected forty penalties in that range or greater.⁷¹ According to one study, penalties have increased by at least 30% year-over-year since 2000, though the Commission’s caseload only grew 3% year-over-year over the same period.⁷²

In a 2006 Statement Concerning Financial Penalties, the SEC said that one of its primary considerations when collecting penalties would be “[t]he degree to which the penalty will recompense or further harm the injured shareholders”;⁷³ regardless, deterring wrongdoers and collecting penalties appeared to be the Commission’s primary objectives.⁷⁴ That same year, one commentator noted that, “[t]oday, a \$10 million SEC penalty would probably be considered a ‘victory’ for most entities settling

63. Atkins & Bondi, *supra* note 21, at 397–98 & n.170.

64. *See id.* at 397–99.

65. *See* Cox & Thomas, *supra* note 1, at 754.

66. *Id.*

67. 15 U.S.C. § 78u-1(a) (2012).

68. *See* STEINBERG & FERRARA, *supra* note 18, § 6.8.

69. *See id.* § 2:1.

70. *See* Atkins & Bondi, *supra* note 21, at 399–400.

71. *Id.* at 400 (citing U.S. SEC. & EXCH. COMM’N, 2004 Performance & Accountability Report (2005), available at <http://www.sec.gov/about/secpar/secpar04.pdf>).

72. *See* Sonia A. Steinway, Comment, *SEC “Monetary Penalties Speak Very Loudly,” But What Do They Say? A Critical Analysis of the SEC’s New Enforcement Approach*, 124 YALE L.J. 209, 209–10 (2014).

73. Press Release, U.S. Sec. & Exch. Comm’n, Statement of the Sec. & Exch. Comm’n Concerning Fin. Penalties (Jan. 4, 2006), available at <http://www.sec.gov/news/press/2006-4.htm>.

74. *See* Steinway, *supra* note 72, at 213–14.

SEC fraud charges.”⁷⁵ Today, the U.S. Treasury General Fund receives a “vast majority” of the sums that the SEC collects, and the Commission contributes more money to that fund than any other government agency.⁷⁶ The following subsections discuss the Dodd-Frank Act and how it united the Commission’s increased emphasis on collecting penalties with an increased emphasis on bringing cases administratively.

A. THE DODD-FRANK ACT

Following a period of economic downturn and political pressure to more strictly regulate financial institutions, President Barack Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) into law in July 2010.⁷⁷ Dodd-Frank expanded the SEC’s authority in a variety of ways.⁷⁸ Most significantly, the Act gave the SEC the authority to pursue monetary penalties against non-regulated entities through administrative proceedings, rather than strictly in federal court.⁷⁹ It gave the SEC more power to impose secondary liability for employees aiding their company’s illegal activity.⁸⁰ It gave the SEC and the Public Company Accounting Oversight Board (PCAOB) more power to regulate foreign private accounting firms.⁸¹ And it allowed the SEC to award whistleblowers with funds not earmarked for disgorgement or the Fair Fund.⁸²

Again, the SEC had already sought such penalty authority in its first 1990 Reform Act proposal.⁸³ But Congress did not want to give the SEC that authority specifically “because the SEC might be perceived to have an incentive to conduct more enforcement actions through its own administrative proceedings.”⁸⁴ Indeed, the SEC now had both the authority and, given the Commission’s increased emphasis on collecting monetary penalties, even greater incentive than it had in 1990 to use internal, administrative proceedings.⁸⁵

75. *Id.* at 210 (citing Paul S. Atkins, Comm’r, U.S. Sec. & Exch. Comm’n, Remarks Before the U.S. Chamber Institute for Legal Reform (Feb. 16, 2006) (transcript available at <http://www.sec.gov/news/speech/spch021606psa.htm>)).

76. *Id.* at 210–11 (citing SEC. & EXCHANGE COMM’N, FY 2014 Congressional Budget Justification 18 n.1 (2014), available at <http://www.sec.gov/about/reports/secfy14congbudgjust.pdf>)).

77. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376, 1802 (2010); see Helene Cooper, *Obama Signs a Contentious Overhaul of the U.S. Financial System*, N.Y. TIMES, July 22, 2010, at B3.

78. *The Dodd-Frank Act Reinforces and Expands SEC Enforcement Powers*, GIBSON DUNN (July 21, 2010), <http://www.gibsondunn.com/publications/pages/Dodd-FrankActReinforcesAndExpandsSECEnforcementPowers.aspx>.

79. See 15 U.S.C. § 77h-1 (2012) (Section 929P(a) of the Dodd-Frank Act amending § 8A of the Securities Act, § 21B(a) of the Securities Exchange Act, § 9(d)(1) of the Investment Company Act, and § 203(i)(1) of the Investment Advisers Act).

80. See *id.*

81. *Id.*

82. See Steinway, *supra* note 72, at 217–18.

83. See Atkins & Bondi, *supra* note 21, at 389–94.

84. *Id.* at 393–94.

85. See Steinway, *supra* note 72, at 213–14.

B. A STATISTICAL OVERVIEW OF SEC ADMINISTRATIVE
PROCEEDINGS, POST-DODD-FRANK

In the years following Dodd-Frank, the SEC began consistently increasing the amount of cases it brought against non-regulated entities through administrative proceedings.⁸⁶ In the fiscal year 2012, the Commission instituted 462 administrative proceedings;⁸⁷ in 2013, 469;⁸⁸ and in 2014, 616.⁸⁹ Even from quarter to quarter of each year, the amount of in-house cases was increasing. One study found that, from January to March 2013, administrative proceedings made up 25% of the SEC's total caseload.⁹⁰ From October to December 2013, however, the study found that they made up 56% of the Commission's caseload.⁹¹ One SEC official commented that it is "fair to say" that the increased use of administrative proceedings is "the new normal."⁹²

86. Different studies of SEC enforcement proceeding statistics find different administrative proceeding totals. Joshua Gallu, *SEC Accounting Doesn't Add Up in 2011 Enforcement Record*, BLOOMBERG BUS. (Mar. 2, 2012), <http://www.bloomberg.com/news/articles/2012-03-02/sec-accounting-of-record-enforcement-year-in-2011-doesn-t-add-up>. Some studies—including the SEC's own in 2011—count "follow-on" administrative proceedings, in which the Commission simply "institute[s] penalties in cases that already had been brought," and "delinquent filings" cases, which do not take the Division of Enforcement as much time to pursue. *Id.* Further, a large number of civil actions and administrative proceedings are settled—though an entity's decision to settle is often motivated by the SEC's impressive win rate. Nearly every study, however, reaches the same general conclusions.

87. *Select SEC and Market Data: Fiscal 2012*, U.S. SEC. & EXCH. COMM'N 3 tbl.3 (2012), <http://www.sec.gov/about/secstats2012.pdf>.

88. *Select SEC and Market Data: Fiscal 2013*, U.S. SEC. & EXCH. COMM'N 3 tbl.2 (2013), <http://www.sec.gov/about/secstats2013.pdf>.

89. *Select SEC and Market Data: Fiscal 2014*, U.S. SEC. & EXCH. COMM'N 3 tbl.2 (2014), <http://www.sec.gov/about/secstats2012.pdf>.

90. Lawrence S. Bader & Peter Janowski, *SEC Enforcement Data Analyses: Analyses of Cases Filed by the SEC in Calendar Year 2014*, MORVILLO ABRAMOWITZ (July 7, 2014), available at <http://www.maglaw.com/publications/articles/00373>.

91. *Id.*

92. Eaglesham, *supra* note 2, at A1.

FIGURE 1.⁹³

SEC Enforcement Action Data: 2005 to 2014												
Administrative Proceedings	294	356	394	386	352	429	469	462	469	610		
AP Percent of Total Actions	47%	62%	60%	58%	53%	63%	64%	63%	69%	81%		
Civil Actions	335	218	262	285	312	252	266	272	207	145		
CA Percent of Total Actions	53%	38%	40%	42%	47%	37%	36%	37%	31%	19%		
Total Actions	630	574	656	671	664	681	735	734	676	755		
	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014		

93. All data were collected from the Select SEC and Market Data annual reports. See *Select SEC and Market Data: Fiscal 2014*, U.S. SEC. & EXCH. COMM'n 3 tbl.2 (2014), <http://www.sec.gov/about/secstats2014.pdf>; *Select SEC and Market Data: Fiscal 2013*, U.S. SEC. & EXCH. COMM'n 3 tbl.2 (2013), <http://www.sec.gov/about/secstats2013.pdf>; *Select SEC and Market Data: Fiscal 2012*, U.S. SEC. & EXCH. COMM'n 3 tbl.3 (2012), <http://www.sec.gov/about/secpar/secpar2012.pdf>; *Select SEC and Market Data: Fiscal 2011*, U.S. SEC. & EXCH. COMM'n 3 tbl.2 (2011), <http://www.sec.gov/about/secstats2011.pdf>; *Select SEC and Market Data: Fiscal 2010*, U.S. SEC. & EXCH. COMM'n 3 tbl.2 (2010), <http://www.sec.gov/about/secstats2010.pdf>; *Select SEC and Market Data: Fiscal 2009*, U.S. SEC. & EXCH. COMM'n 3 tbl.2 (2009), <http://www.sec.gov/about/secstats2009.pdf>; *Select SEC and Market Data: Fiscal 2008*, U.S. SEC. & EXCH. COMM'n 3 tbl.2 (2008), <http://www.sec.gov/about/secstats2008.pdf>; *Select SEC and Market Data: Fiscal 2007*, U.S. SEC. & EXCH. COMM'n 3 tbl.2 (2007), <http://www.sec.gov/about/secstats2007.pdf>; *Select SEC and Market Data: Fiscal 2006*, U.S. SEC. & EXCH. COMM'n 3 tbl.2 (2006), <http://www.sec.gov/about/secstats2006.pdf>; *Select SEC and Market Data: Fiscal 2005*, U.S. SEC. & EXCH. COMM'n 3 tbl.2 (2005), <http://www.sec.gov/about/secstats2005.pdf>.

As one might expect, the SEC was experiencing much greater success in its administrative proceedings than it was in federal court.⁹⁴ In fiscal year 2014, during which the SEC began its yearlong 100% administrative proceeding win streak, the Commission won only 61% of the cases that it brought in federal court.⁹⁵ That same year, the SEC won all six administrative hearings that came to verdict.⁹⁶ By contrast, the Commission won only 11 out of 18 cases in district court.⁹⁷ Finally, a recent Wall Street Journal study found that from October 2010 to March 2015, the SEC won 90 percent of contested cases that progressed before an administrative law judge compared to a 69 percent success rate in federal court over the same timeframe.⁹⁸ Respondents' appeals to SEC administrative decisions fared worse: "[t]he [SEC] commissioners decided in their own agency's favor concerning 53 out of 56 defendants in appeals—or 95%—from January 2010 through [March 2015]."⁹⁹

IV. AN ANALYSIS OF SEC ADMINISTRATIVE ENFORCEMENT, POST-DODD-FRANK

Thus, following several significant pieces of legislation, the SEC has clearly strayed far from the philosophy that its Division of Enforcement embraced in the 1990s, when the SEC originally received the power to pursue monetary penalties for most securities law violations.¹⁰⁰

Given the SEC's increased use of administrative proceedings and its success in those proceedings (compared to its success in district court), some commentators and practitioners began to question the fairness of the in-house court system.¹⁰¹ Some focused on the fact that the judges were on the SEC's payroll and how unlikely it is that federal judges would reverse an ALJ's decision.¹⁰² Others focused on the SEC's Rules of Practice and the ways in which the quick discovery and decision periods, among other things, disadvantaged respondents.¹⁰³ One Manhattan federal judge said that, with its use of administrative courts, the SEC was becoming "a law unto itself" and added he saw no reason to replace fed-

94. See Morgenson, *supra* note 7.

95. See Nate Raymond, *U.S. Judge Criticizes SEC Use of In-House Court for Fraud Cases*, REUTERS (Nov. 5, 2014, 1:37 PM), <http://www.reuters.com/article/2014/11/05/sec-fraud-rakoff-idUSL1N0SV2LN20141105>.

96. See *Heading to Court, but Which One?*, INVESTMENT NEWS (Mar. 1, 2015 12:01 AM), <http://www.investmentnews.com/article/20150301/REG/303019994/heading-to-court-but-which-one>.

97. See *id.*

98. See Jean Eaglesham, *In-House Judges Help SEC Rack Up Wins — Success rate for agency is 90%, and if it loses, it can appeal to its commissioners*, WALL ST. J., May 7, 2015, at A1.

99. *Id.*

100. See Atkins & Bondi, *supra* note 21, at 392.

101. See Morgenson, *supra* note 7 (noting that, "[a]s a securities lawyer, I've been involved in these administrative proceedings for many years and have been struck by the unfairness and lack of neutrality in the system The judges' mind-set reflects the agenda of the agency, which in this arena is enforcement").

102. See *id.*

103. See Henning, *supra* note 3.

eral courts with “administrative fiat.”¹⁰⁴

More recently, several respondents have lodged constitutional challenges to the administrative system.¹⁰⁵ The SEC denies that its current procedures are improper,¹⁰⁶ but as it shifts more enforcement actions in-house, the critics will only grow louder. The following subsections will analyze the problems with the SEC’s use of the administrative proceedings as they exist today.

A. DISTRICT COURT STANDING FOR CONSTITUTIONAL CHALLENGES

Respondents that challenge these administrative proceedings on constitutional grounds first deal with the threshold issue of whether they must exhaust their administrative remedies before seeking recourse in federal court. So far, they have experienced mixed success.¹⁰⁷ Federal courts have original jurisdiction over claims arising under the Constitution.¹⁰⁸ However, Congress can evidence an intent to restrict that original jurisdiction if the “‘statutory scheme’ displays a ‘fairly discernible’ intent to limit jurisdiction, and the claims at issue ‘are of the type Congress intended to be reviewed within th[e] statutory structure.’”¹⁰⁹ In order for a constitutional claim against the SEC to receive an immediate ruling, therefore, (1) “a finding of preclusion could foreclose all meaningful judicial review;” (2) the claim must be “wholly collateral to a statute’s review provisions;” and (3) the claims must be “outside the agency’s expertise.”¹¹⁰

The first two prongs of this test, drawn from *Thunder Basin Coal Co. v. Reich*,¹¹¹ have so far proved formidable stumbling blocks for administrative respondents.

In *Gupta v. S.E.C.*, a New York district court said that the administrative respondent had standing to bring his equal protection¹¹² challenge in federal court.¹¹³ First, the court said the SEC ALJ’s expertise did not encompass constitutional challenges such as Gupta’s.¹¹⁴ Second, Gupta alleged the SEC “irrationally and illegally” singled him out for an admin-

104. See Raymond, *supra* note 95 (internal quotations omitted).

105. See generally Complaint, *Duka v. S.E.C.*, No. 15-357 (S.D.N.Y. Jan. 16, 2015); Complaint, *Bebo v. S.E.C.*, No. 15-00003 (E.D. Wis. Jan. 2, 2015); Complaint, *Stilwell v. S.E.C.*, No. 14-07931 (S.D.N.Y. Oct. 1, 2014); Complaint, *Gray Fin. Grp., Inc. v. S.E.C.*, No. 1:15-cv-0492-CAP (N.D. Ga. Feb. 19, 2015).

106. Andrew Ceresney, Director, Division of Enforcement, U.S. Sec. & Exch. Comm’n, Remarks to the American Bar Association’s Business Law Section Fall Meeting (Nov. 21, 2014), available at <http://www.sec.gov/News/Speech/Detail/Speech/1370543515297#.VMnnAWjF9zM>.

107. See *Chau v. S.E.C.*, No. 14-CV-1903, 2014 WL 6984236 (S.D.N.Y. Dec. 11, 2014); see also *Gupta v. S.E.C.*, 796 F. Supp. 2d 503 (S.D.N.Y. 2011).

108. 28 U.S.C. § 1331.

109. *PCAOB*, 561 U.S. at 489 (quoting *Thunder Basin Coal Co. v. Reich*, 510 U.S. 200, 207, 212 (“Thunder Basin”) (1994)).

110. *Id.*

111. *Thunder Basin*, 510 U.S. at 207, 212.

112. See U.S. CONST. amend. V.

113. See *Gupta v. S.E.C.*, 796 F. Supp. 2d at 503.

114. *Id.* at 512.

istrative proceeding out of a host of defendants.¹¹⁵ The court found that claim satisfied the wholly collateral requirement because Gupta would have an equal protection requirement regardless of whether he received an adverse ALJ ruling.¹¹⁶ Before Gupta received a ruling on the merits of his claim, however, the SEC voluntarily terminated its administrative action and refiled in federal court.¹¹⁷

Though the Second Circuit has never discussed the ruling's merits, the *Gupta* decision has only been cited negatively by sister courts.¹¹⁸ In *Chau v. S.E.C.*, the administrative respondent asserted both due process and equal protection claims, but the district court ruled it did not have subject-matter jurisdiction over those claims.¹¹⁹ First, it said *Gupta* properly resisted a "black-and-white" rule and that "the question of whether a special statutory scheme provides for adequate review of administrative actions involves case-specific determinations."¹²⁰ But the due process claim—that respondent did not have enough time to prepare for the proceeding—was not collateral primarily because the claim was "central to [the agency's] day-to-day conduct" within the case.¹²¹ In addition, both claims fell within agency expertise, and the court seemed persuaded by the fact that Chau could eventually attain standing in federal court after he exhausted his administrative remedies via 15 U.S.C. 78y, which states:

A person aggrieved by a final order of the Commission entered pursuant to this chapter may obtain review of the order in the United States Court of Appeals for the circuit in which he resides or has his principal place of business, or for the District of Columbia Circuit, by filing in such court, within sixty days after the entry of the order, a written petition requesting that the order be modified or set aside in whole or in part.¹²²

The ongoing case of *S.E.C. v. Bebo* addressed for the first time the issue of Appointments Clause challenge standing in federal court prior to the exhaustion of administrative remedies.¹²³ The results were decidedly mixed: the district court judge labeled the administrative respondent's claims "compelling and meritorious" but said that "whether [the equal protection claim] is correct cannot be resolved here."¹²⁴ The court ruled that the administrative respondent must first litigate the claims before the SEC and then, if necessary, on appeal to the Court of Appeals for the

115. *Id.*

116. *Id.* at 513.

117. See Henning, *supra* note 3.

118. See *Salazar v. Duncan*, No. 14-1230, 2015 WL 252078 (S.D.N.Y. Jan. 16, 2015); see also *Chau v. S.E.C.*, No. 14-CV-1903, 2014 WL 6984236 (S.D.N.Y. Dec. 11, 2014).

119. See *Chau*, 2014 WL 6984236.

120. *Id.* at *5.

121. *Id.* at *9.

122. *Id.* at *11–13.

123. See generally *Bebo v. S.E.C.*, No. 15-C-3, 2015 WL 905349 (E.D. Wis. Mar. 3, 2015).

124. *Id.* at *2.

Seventh Circuit.¹²⁵

The court applied the three-prong *Thunder Basin* test, it held that a finding of preclusion would not foreclose all meaningful judicial review, and it distinguished *Bebo* from *Free Enterprise Fund v. Public Company Accounting Oversight Board (PCAOB)*,¹²⁶ in which no agency review was required prior to review of an Appointments Clause claim in federal court, in several ways.¹²⁷ First, it noted that in *PCAOB*, the SEC had no action pending against the plaintiffs, and the plaintiffs would otherwise have to induce SEC action to open up a pathway to agency review.¹²⁸ Further, not every Board action is encapsulated in a final Commission order or rule.¹²⁹ By contrast, *Bebo* would not have to induce an administrative proceeding, and ever ALJ ruling is made final when it is issued by the Commission.¹³⁰ And if the SEC's final order did not resolve *Bebo*'s claims to her satisfaction, "the Exchange Act [in 15 U.S.C. 78y] provides that a 'person aggrieved' by a final SEC order 'may obtain review of the order in the United States Court of Appeals for the circuit in which he resides or has his principal place of business.'"¹³¹

The appeals statute, § 78y, is the trump card to all of these requests for federal court review prior to the exhaustion of all administrative remedies¹³². The Commission's ALJs can address the constitutional arguments in a motion for summary within the administrative proceeding, as an ALJ later suggested in *Bebo*'s case, and an appeals court will hear the claim of a dissatisfied administrative respondent if the respondent files a timely post-order appeal.¹³³ Therefore, meaningful judicial review will virtually always exist, and the claim would fail the first prong of the *Thunder Basin* test.

In *Hill v. SEC*, the federal court found that it did have jurisdiction to review the plaintiff's Appointments Clause claims because § 78y did not, in fact, provide meaningful judicial review.¹³⁴ This case was significant because it was the first in which a federal judge held both that the court had jurisdiction over a constitutional claim and that the plaintiff was likely to succeed on the merits of that claim.¹³⁵ The court reached its jurisdictional conclusion by pointing out that "delayed judicial review here will cause an allegedly unconstitutional process to occur."¹³⁶ But this ruling seems like a strained interpretation of the "meaningful judicial re-

125. *Id.*

126. *See generally* *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd. (PCAOB)*, 561 U.S. 477 (2010).

127. *Bebo*, 2015 WL 905349, at *2–4.

128. *Id.* at *2–3.

129. *Id.*

130. *Id.*

131. *Id.* at *2; *see* 15 U.S.C. § 78y(a)(1) (2012).

132. *See generally* 15 U.S.C. § 78y.

133. *Id.*

134. *See* Order, *Hill v. S.E.C.*, No. 15-cv-1801-LMM (N.D. Ga. 2015).

135. *See id.*

136. *Id.* at 18.

view” test. It is true that the allegedly unconstitutional process will have occurred, but the administrative ruling can then be appealed to federal court and dealt with appropriately. If the federal court can later hear the case and later undo the effects of an unconstitutional process, “meaningful judicial review” will have occurred.

However, strong policy reasons still exist for immediate federal court review. For both regulated and non-regulated entities, winning a securities case in federal court after the exhaustion of all other remedies may be “little more than a Pyrrhic victory.”¹³⁷ All the clients and business will have already left, and the respondent will have nothing left to fight for. If an administrative respondent could prove that such a scenario would come to pass by the end of the Commission’s proceedings, the respondent could argue that judicial review would no longer be meaningful. Immediate federal review on a case-by-case basis would provide a check to that problem.

B. DUE PROCESS AND EQUAL PROTECTION ISSUES

Since Dodd-Frank, at least four respondents in SEC administrative proceedings have argued in their district court requests for injunction that the SEC’s administrative proceedings fail to adequately protect their Equal Protection and Due Process rights.¹³⁸ Primarily, their equal protection complaints have alleged that the SEC “intentionally treated differently from others similarly situated and that there is no rational basis for the disparate treatment.”¹³⁹ The due process complaints, often coupled with equal protection challenges, allege that the SEC chose the administrative forum because the Commission could not sustain the evidentiary burdens of federal court and because other procedural devices, such as the accelerated procedural speed, give the Commission an insurmountable advantage.¹⁴⁰ Such procedural complaints are valid in many cases, and district courts should examine the validity of due process claims by considering how the SEC typically handles similar cases and how greatly the forum disadvantaged the respondent.

1. Due Process Challenges and Procedural Disadvantages

Some administrative respondents advance another fairly straightforward argument: that the SEC’s administrative proceedings lack signifi-

137. See Steinway, *supra* note 72, at 213–14 (citing Linda Greenhouse, *Justices Unanimously Overturn Conviction of Arthur Andersen*, N.Y. TIMES, May 31, 2005, <http://www.nytimes.com/2005/05/31/business/31wire-andersen.html>).

138. See Complaint at 1–5, *Bebo v. S.E.C.*, No. 15-00003 (E.D. Wis. 2015); see also *Chau v. S.E.C.*, No. 14-CV-1903, 2014 WL 6984236 (S.D.N.Y. Dec. 11, 2014); *Peixoto v. S.E.C.*, No. 14-8364 (S.D.N.Y. 2014); *Gupta v. S.E.C.*, 796 F. Supp. 2d 503, 514 (S.D.N.Y. 2011).

139. *Chau*, 2014 WL 6984236 at *10 n. 110 (citing *Vill. of Willowbrook v. Olech*, 528 U.S. 562, 564 (2000); *Engquist v. Or. Dep’t of Agric.*, 553 U.S. 591, 603 (2008) (restricting “class of one” claims in the public employment context, in part based on the “discretion that [public employers] are entrusted to exercise”)).

140. See Complaint at 1–5, *Bebo v. S.E.C.*, No. 15-00003 (E.D. Wis. 2015).

cant procedural protections afforded in federal court to a degree that violates the Constitution's due process clause. At least one New York federal district court judge, Judge Jed Rakoff, has made comments suggesting he'd be willing to entertain such an argument.¹⁴¹ Rakoff noted in particular that it would be unwise to displace a "constitutional alternative with administrative fiat." The Commission's ALJs may soon have a much greater influence on securities law doctrine's development, he said, because of how the SEC's procedural rules disadvantage administrative respondents, because of the SEC's increased preference for administrative proceedings, and because of the deference federal courts afford agencies.¹⁴² That is unfair to administrative respondents and federal court defendants alike.

a. ALJ Decision Deadlines

The SEC administrative courts' unrealistic time constraints relating to decision issuances are perhaps the forum's most prominent procedural disadvantage.¹⁴³ Commission ALJs have either 120, 200, or 300 days from service to render an initial decision, and the SEC decides which of those three timelines it wants generally based on the complexity of the matter and the need for expediency.¹⁴⁴ Everything between service and decision must be completed within that period: "[d]iscovery, trial preparation, pre-hearing conferences, the hearing itself, post-hearing briefing, and submission of proposed findings of fact and conclusions of law."¹⁴⁵ Unless they ask for an extension, ALJs must issue a decision by the prescribed deadline, whereas federal judges follow no statutorily imposed deadline.¹⁴⁶ This problem will only worsen now that the SEC is bringing disclosure and financial reporting fraud in-house.¹⁴⁷

Another problem related to proceeding speed is that the post-service time for settlement negotiations is compressed.¹⁴⁸ And, unlike ALJs, district court judges work with magistrate judges who can oversee those negotiations.¹⁴⁹ Given all of these time pressures, administrative respondents are more likely to settle, even if they think that their case has merit.

141. Raymond, *supra* note 95.

142. *Id.*

143. See Henning, *supra* note 3.

144. SEC Rule of Practice 360(a)(2).

145. Alan M. Lieberman, *Fast-Track Justice: Is The SEC Exercising 'Unchecked And Unbalanced Power'?*, 20 No. 10 WESTLAW J. SEC. LITIG. & REG. 1, at *3 (Sept. 18, 2014).

146. *Id.*

147. *Id.* at *4 (citing *In re Airtouch Commc'ns*, AP File No. 3-16033 (2014); *In re Cummings*, AP File No. 3-15991 (2014); *In re Sherman*, AP File No. 3-15992 (2014); *In re Neely*, AP File No. 3-15945 (2014)).

148. *Id.* at *3.

149. See Lieberman, *supra* note 145, at *5.

b. Discovery Limitations

Additionally, discovery is greatly limited because respondents cannot conduct depositions of expert witnesses and because the ALJ has discretion to allow all other witnesses to be deposed.¹⁵⁰ In order to conduct any depositions, the respondent must submit a “written motion setting forth the reasons why such deposition should be taken, including the specific reasons why the party believes the witness will be unable to attend or testify at the hearing.”¹⁵¹ Thus, if the SEC has already talked with a fact witness and the ALJ deems a deposition unnecessary, a respondent, who lacks subpoena power, must independently contact the witness for an informal conversation.¹⁵²

And because of the decision issuance deadlines, petitioners are at a disadvantage in gathering documents and getting in touch with potential witnesses.¹⁵³ While the SEC may take months or years to prepare their case, the accused’s discovery clock starts upon service.¹⁵⁴ Respondents are therefore not only forced to anticipate that the SEC will file an action against them but also that the Commission will do so administratively.¹⁵⁵

Other jurisdictional problems with administrative discovery rights exist. In *Bebo v. S.E.C.*, an action requesting injunction that is pending in federal court, the administrative respondent alleges that the proceedings infringe on its individual due process rights because five important witnesses reside in Canada.¹⁵⁶ The SEC administrative court’s subpoena powers do not extend beyond the United States, whereas in federal court, it could submit letters rogatory and very likely obtain the deposition testimony sought.¹⁵⁷ Such circumstances could at least tempt the SEC to bring a case administratively when the Commission knows that doing so will deprive the administrative respondent access to key witnesses.

c. Absence of a Right to Trial by Jury

Additionally, respondents in these proceedings have no right to trial by jury.¹⁵⁸ That right is guaranteed by the U.S. Constitution¹⁵⁹ and the Fed-

150. RP 233(a–b), 17 C.F.R. § 201.233(a–b) (2015); see Lieberman, *supra* note 145, at *3–4.

151. RP 233(a), 17 C.F.R. § 201.233(a) (2015).

152. William F. Johnson & Amelia R. Medina, *SEC’s Administrative Enforcement Intensifies Fairness Debate*, N.Y. L.J. (Nov. 6, 2014), <http://www.newyorklawjournal.com/id=1202675574765/SECs-Administrative-Enforcement-Intensifies-Fairness-Debate?slreturn=20150029200035>.

153. *Id.*

154. *Id.*

155. *Id.*

156. See Complaint at 24–25, *Bebo v. S.E.C.*, No. 15-00003 (E.D. Wis. 2015).

157. See *id.* (citing 15 U.S.C. § 78u(b), which only authorizes “attendance of witnesses and the production of any such records . . . from any place in the United States or any State”).

158. Johnson & Medina, *supra* note 152.

159. U.S. CONST. amend. VII.

eral Rules of Civil Procedure in certain federal court proceedings.¹⁶⁰ As one administrative respondent pointed out in its federal pleading, “the legislative history regarding Section 929P(a)¹⁶¹ of Dodd-Frank confirms that . . . Congress[]” specifically provided the SEC with an administrative cause of action directly parallel to a federal cause of action.¹⁶² The history reflects that Section 929P(a) makes “the SEC’s authority in administrative penalty proceedings coextensive with its authority to seek penalties in federal court.”¹⁶³ Therefore, a government agency can pursue the same cause of action in two venues, and depending on the government agency’s choice of venue, a respondent may or may not have the constitutional right to trial by jury. If the government’s sole purpose is “to discourage the assertion of constitutional rights[,] it is ‘patently unconstitutional.’”¹⁶⁴ Here, the SEC has removed the chance to assert an “inviolable” constitutional right altogether and the SEC receives no disadvantage for that removal.¹⁶⁵ When an administrative respondent is the only case among many arising out of the same cause of action and when a jury would clearly favor the respondent, an issue of Equal Protection exists.

d. Looser Evidentiary Standards

Further, ALJs have broad discretion to introduce evidence, including hearsay, that would not be admitted in federal court.¹⁶⁶ These looser standards often result in administrative proceedings being “based on purely circumstantial evidence, sometimes without a single witness who can relate firsthand knowledge of any wrongdoing by the respondent.”¹⁶⁷ At least one commentator has labeled this rule as neutral in theory but an “entirely one-sided” investigative examination in practice.¹⁶⁸ This is especially true given that the respondent may not be able to depose those witnesses before the proceeding.¹⁶⁹ This problem, along with all the due process problems that this Article discusses, is compounded by the fact that Commission-reviewed ALJ decisions enjoy considerable deference upon appeal to a court of appeals.¹⁷⁰

160. See FED. R. CIV. P. 38(a) (“The right of trial by jury as declared by the Seventh Amendment to the Constitution—or provided by a federal statute—is preserved to the parties inviolate.”).

161. Pub. L. No. 111-203 § 27(b), 124 Stat. 1376 (2010).

162. See Complaint at 22, *Bebo v. S.E.C.*, No. 15-00003, at 22 (E.D. Wis. Jan. 2, 2015).

163. H.R. REP. NO. 111-687, at 78 (2010).

164. *Chaffin v. Stynchcombe*, 412 U.S. 17, 32 n.20 (1973).

165. See Lieberman, *supra* note 145, at *4.

166. S.E.C. Rules of Practice 320, 17 C.F.R. § 201.233 (2006); see, e.g., *In re Fortenberry*, Adm. Proc. File No. 3-15858, at *2 (2014) (“[E]vidence is presumptively admissible.”).

167. Johnson & Medina, *supra* note 152.

168. Lieberman, *supra* note 145, at *4.

169. S.E.C. Rules of Practice 233(a), 17 C.F.R. § 201.233(a).

170. *Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837, 844–45 (1984) (holding that “a court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency”).

2. Equal protection claims

Several administrative respondents have premised equal protection claims on the fact that “it was constitutionally improper for the SEC to pursue charges against [them] administratively while bringing similar cases in Article III courts.”¹⁷¹ Plaintiffs draw this claim primarily from *Village of Willowbrook v. Olech* in which the Supreme Court held that “successful equal protection claims [may be] brought by a ‘class of one,’ where the plaintiff alleges that she has been intentionally treated differently from others similarly situated and that there is no rational basis for the difference in treatment.”¹⁷² Thus, even if the SEC had the discretion to pursue a particular claim in administrative court, the SEC may not necessarily be entitled to that choice of venue if it treated a respondent unequally and if “the unequal treatment was still arbitrary and irrational.”¹⁷³

The merits of these claims have not yet been decided. The plaintiff in *Gupta* successfully established standing in part because he was the only one of twenty-nine associated parties whose case was brought administratively.¹⁷⁴ However, the court in *Chau* distinguished its equal protection claim from *Gupta* primarily because *Chau* could only identify three associated parties whose cases weren’t brought administratively, though the merits of the claim were not actually decided since the court held it had no jurisdiction over the claim.¹⁷⁵

3. Chevron deference

Once these due process and equal protection claims gain standing in federal court, however, they must overcome the great deference that federal courts afford agencies like the SEC, derived from the Supreme Court’s decision in *Chevron v. Natural Resources Defense Council*.¹⁷⁶ This landmark administrative decision stands for the proposition that “a court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency.”¹⁷⁷ Federal judges, particularly in the lower courts, will not be eager to rule against the SEC on either of these grounds, particularly. Ultimately, the primary problem with any due process claim is that Congress knowingly gave the SEC the power to establish these procedural rules. And the primary problem with almost any equal protections claim is that Congress knowingly gave the SEC the authority to choose its litigation forum.

171. *Chau v. S.E.C.*, 2014 WL 6984236 at *10.

172. *Vill. of Willowbrook v. Olech*, 528 U.S. 562, 564–66 (2000); *see also* *Engquist v. Or. Dep’t of Agric.*, 553 U.S. 591, 603 (2008).

173. *Gupta v. S.E.C.*, 796 F. Supp. 2d 503, 513 (S.D.N.Y. 2011).

174. *Id.*

175. *Id.* at *10.

176. *See generally* *Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837 (“*Chevron*”) (1984).

177. *Id.* at 844–45.

Thus, the SEC and Congress may ultimately need to be the ones who provide the remedy for these issues.

C. APPOINTMENTS CLAUSE ISSUES

Several other petitioners have lodged broader constitutional attacks¹⁷⁸ that focus on whether the SEC's in-house judges are inferior executive officers and whether the president retains sufficient authority over the Commission's ALJs under the Constitution's Appointments Clause.¹⁷⁹ This subsection will analyze the Supreme Court's recent decision in *Free Enterprise Fund v. Public Company Accounting Oversight Board (PCAOB)*¹⁸⁰ and discuss why the court found that ALJs are inferior executive officers and why the decision dictates that the ALJs' two layers of for-cause protection render them unable to preside over the SEC's administrative proceedings.

1. Analyzing *Free Enterprise Fund v. PCAOB*

The Constitution's Appointments Clause states that the President: shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law: but the Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Court of Law, or in the Heads of Departments.¹⁸¹

Though the Appointments Clause says nothing specifically about the President's removal powers, courts have interpreted it to mean that the President should retain a reasonable amount of control over the removal of inferior executive officers—as opposed to superior executive officers under the President's direct control.¹⁸² The Supreme Court has repeatedly held that for-cause removal, afforded to either the inferior officer or the officer supervising that inferior officer, is constitutional.¹⁸³

Generally speaking, *PCAOB* examined whether a scheme that affords both the inferior officer and the officer for-cause removal protection is constitutional under the Appointments Clause.¹⁸⁴ In that case, the SEC commissioners could only be removed by the president for good cause,

178. See generally Complaint, *Duka v. S.E.C.*, No. 15-357 (S.D.N.Y. 2015); Complaint, *Bebo v. S.E.C.*, No. 15-00003 (E.D. Wis. 2015); Complaint, *Stilwell v. S.E.C.*, No. 14-07931 (S.D.N.Y. 2014); *Gray Fin. Grp., Inc. v. S.E.C.*, No. 1:15-cv-0492-CAP (N.D. Ga. 2015); *Tilton v. S.E.C.*, No. 15-cv-02472.

179. U.S. CONST. art. II, § 2.

180. *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd. ("PCAOB")*, 561 U.S. 477 (2010).

181. U.S. CONST. art. II, § 2.

182. *PCAOB*, 561 U.S. at 478–79.

183. *Id.* at 494.

184. *Id.* at 477.

and the commissioners could only remove the PCAOB members for good cause.¹⁸⁵ First, the SEC held that the PCAOB were inferior officials who exercised executive authority.¹⁸⁶ Then, the Supreme Court said the second layer of for-cause protection prevents the president from holding the “[SEC] fully accountable for the Board’s conduct, to the same extent that he may hold the [SEC] accountable for everything else that it does” because the SEC is “not responsible for the Board’s actions,” but only “for their own determination of whether the Act’s rigorous good-cause standard is met.”¹⁸⁷ Chief Justice Roberts, who authored the opinion, did not strike down the entire PCAOB system but rather simply held that the second layer of protection, insulating the PCAOB, was unconstitutional.¹⁸⁸ Further, he specifically side-stepped the issue of whether *PCAOB* would apply to ALJs, leaving the case’s applicability to the SEC’s in-house judges up for debate.¹⁸⁹

2. Applying *Free Enterprise Fund v. PCAOB*

One commentator distilled the *PCAOB* decision into a four-part test, under which this comment will analyze the constitutional validity of the Commission ALJs’ authority: “(1) Is an inferior officer separated from presidential removal by two or more layers of for-cause protection? . . . (2) Does the inferior officer exercise substantial executive authority? . . . (3) Can the inferior officer be removed for conduct that is not directly related to his employment? . . . (4) Can the President initiate removal proceedings?”¹⁹⁰

a. Are SEC Administrative Law Judges Officers?

Chief Justice Roberts said that the officer status of ALJs is in question, indicating that they might also be considered employees.¹⁹¹ However, prior Supreme Court opinions have generally come to the opposite conclusion, though no majority opinion has explicitly said so. As Justice Breyer pointed out in his dissent, quoting Justice Scalia’s concurring opinion in *Freytag v. Commissioner*, ALJs “are all executive officers.”¹⁹² The ALJs’ duties also comport with the definition of an officer provided by the Office of Legal Counsel of the Department of Justice: “if (1) [the

185. *Id.* at 486–87.

186. *Id.* at 495.

187. *Id.* at 496–97.

188. *Id.* at 509–10.

189. *Id.* at 507 n.10.

190. David Moon, Note, *When Does Dual For-Cause Removal Protection Become Unconstitutional? Exploring the Scope of Free Enterprise Fund v. Public Company Accounting Oversight Board*, 2013 WIS. L. REV. 875, 899 (2013).

191. *PCAOB*, 561 U.S. at 507 n.10.

192. *Id.* at 542 (Breyer, J., dissenting) (citing *Freytag v. Comm’r*, 501 U.S. 868 (1991) (opinion concurring in part and concurring in judgment) (emphasis deleted)); *id.* at 868 (majority opinion) (“[A] [tax-court] special trial judge is an ‘inferior Officer.’”); *Edmond v. United States*, 520 U.S. 651, 663 (1997) (“[M]ilitary trial and appellate judges are [inferior] officers.”).

person] is invested by legal authority with a portion of the sovereign powers of the federal Government, and (2) [the person's authority] is 'continuing,' " that person is an officer.¹⁹³ Finally, the ALJs are inferior officers by virtue of Justice Scalia's simple test in *Edmond v. United States*: they are officers, and they have superiors who "were appointed by presidential nomination with the advice and consent of the Senate."¹⁹⁴

The SEC might argue that its administrative law judges' inferior officer status should be analyzed through the lens of *Landry v. Federal Deposit Insurance Corp.*¹⁹⁵ In that case, the D.C. Circuit Court held that under *Freytag*, the FDIC ALJs were not inferior officers because they did not have the authority to render final decisions in certain classes of cases. However, the concurrence correctly pointed out that "[o]nly after it concluded [special trial judges] were inferior officers did *Freytag* address the STJ's ability to issue a final order; the STJ's limited authority to issue final orders was only an additional reason, not the reason."¹⁹⁶ Thus, the SEC judges' decisions must be approved by a majority of SEC commissioners, but under *Freytag*, that fact is not dispositive. Because of all the Commission's ALJs' powers detailed in previous sections of this article, the judges exercise significant authority and are inferior officers.

b. Are the ALJs Separated from Presidential Removal By Two or More Layers of For-Cause Protection?

The Commission's ALJs can be removed from their position "only" for "good cause," as "established and determined" by the Merit Systems Protection Board (MSPB).¹⁹⁷ The SEC commissioners, who exercise removal power, cannot be removed by the President except for "inefficiency, neglect of duty, or malfeasance in office."¹⁹⁸ Finally, the MSPB, which reviews the exercise of that removal power, can be removed by the President "only for inefficiency, neglect of duty, or malfeasance in office."¹⁹⁹ Therefore, it appears that the ALJs receive at least two layers of for-cause removal protection. These statutes also indicate (1) that the inferior officers, the ALJs, cannot be removed for conduct that is not directly related to their employment and (2) that the President cannot initiate removal proceedings.²⁰⁰ Further attenuating the ALJs' connection to the president, the SEC Commissioners cannot appoint the judges without the prior approval of the SEC's Office of Personal Manage-

193. Officers within the Meaning of the Appointment Clause, 31 Op. O.L.C. 1 (2007), available at <http://www.justice.gov/sites/default/files/olc/opinions/2007/04/31/appointmentsclausev10.pdf>.

194. See *Edmond v. United States*, 520 U.S. 651, 663 (1997).

195. *Landry v. Fed. Deposit Ins. Corp.*, 204 F.3d 1125 (D.C. Cir. 2000).

196. See *Hill v. S.E.C.* (generally citing *Landry*, 204 F.3d at 1140, 1141).

197. 5 U.S.C. § 7521(a) (2012).

198. See *PCAOB*, 561 U.S. at 487; see also *MFS Sec. Corp. v. S.E.C.*, 380 F.3d 611, 619–20 (2d Cir. 2004).

199. 5 U.S.C. § 1202(d) (2012).

200. See 5 U.S.C. §§ 1202(d), 7521(a).

ment.²⁰¹ That leaves only one hurdle.

c. Do the ALJs Exercise Substantial Executive Authority?

The “substantial executive authority” step—discussing whether ALJs are executive officers despite their traditionally adjudicative functions—inspired a most spirited Supreme Court debate. In a footnote, Chief Justice Roberts indicated that he did not believe the *PCAOB* ruling applied to ALJs²⁰² because, “unlike members of the Board, many administrative law judges of course perform adjudicative rather than enforcement or policymaking functions, or possess purely recommendatory powers.”²⁰³ Justice Breyer disagreed, warning that the *PCAOB* ruling could provide a legitimate basis on which respondents could challenge many ALJ systems.²⁰⁴ Breyer took issue with Roberts’s assertion that the Board does not perform adjudicative functions because Breyer believed that the PCAOB did perform some adjudicative functions, such as disciplining and sanctioning, alongside its executive and legislative functions.²⁰⁵ And absent that distinguishing “adjudicative function” factor, the Commission’s ALJ two-layer system of for-cause protection appears unconstitutional.

However, at least one commentator suggests that Chief Justice Roberts distinguished the PCAOB and ALJs because the ALJs perform “purely” adjudicative functions—presumably making appropriate the additional insulation from the threat of removal—whereas the PCAOB performed a mixture of adjudicative, executive, and legislative functions.²⁰⁶ However, that commentator also concedes that such a reading requires inserting a parenthetical “in addition” into Chief Justice Roberts’s footnote, causing it to read: “unlike members of the Board, many administrative law judges of course perform adjudicative rather than [in addition to their] enforcement or policymaking functions.”²⁰⁷

It is possible to read into Roberts’s footnote a legal distinction between the PCAOB and ALJs, but that distinction cannot be found in the plain language of the opinion. Such a reading requires the insertion of an awkward but obvious parenthetical. Reading the plain language of the opinion, it appears that Justice Breyer’s interpretation is correct. Chief Justice Roberts simply made a forced, incorrect analysis about the PCAOB’s du-

201. 5 C.F.R. § 930.204 (“An agency may appoint an individual to an administrative law judge position only with prior approval of OPM, except when it makes its selection from the list of eligibles provided by OPM. An administrative law judge receives a career appointment and is exempt from the probationary period requirements under part 315 of this chapter.”).

202. Likewise, the SEC stresses that its ALJs are independent *judicial* officers. See *Office of Admin. Law Judges, About the Office*, U.S. SEC. & EXCH. COMM’N, <http://www.sec.gov/alj> (last updated Nov. 25, 2014).

203. *PCAOB*, 561 U.S. at 507 n.10.

204. See *id.* at 541–45 (Breyer, J., dissenting).

205. See *id.* at 530–31.

206. Kevin M. Stack, *Agency Independence After PCAOB*, 32 *CARDOZO L. REV.* 2391, 2048, 2412 n.117 (2011).

207. *Id.* (citation omitted).

ties. Were this issue of the SEC administrative system's validity taken to the Supreme Court, it is possible that the Court would still distinguish the Commission's ALJs based on policy concerns, such as the need to "insulate those with adjudicative functions with good-cause removal protections."²⁰⁸ But the *PCAOB* decision does not itself provide sufficient grounds for such a differentiation, and lower courts should therefore rule in favor of respondents' Appointments Clause challenges.

Even if a court decided in an administrative respondent's favor on an Appointments Clause challenge, however, the court would likely follow other courts' lead and remove the SEC ALJs' for-cause protection. The case would then probably be remanded back to the in-house court from which the respondent sought to escape. Thus, while such challenges might deter the SEC from bringing a case administratively, they are not an end solution to the core problem.

D. INCREASED EMPHASIS ON "WINNING" AND COLLECTING MONETARY PENALTIES

The SEC's current administrative court system is also problematic purely as a policy matter because it places far too much significance on simply winning cases and collecting monetary penalties for minimum costs, rather than deterring future illegal action and protecting the public. The problem is, winning and quick settlements often do little to deter future illegal conduct when non-regulated entities see settlements as a cost of doing business. To its credit, the Commission emphasized in 2013 that it would ask for accompanying admissions of guilt with settlement in a broader range of cases.²⁰⁹ But contemporaneously, the Commission also said that "the majority of cases will continue to be resolved on a no admit no deny basis, as the interest in quick resolutions and settlements will, in most cases, outweigh the interests in obtaining admissions."²¹⁰ And it appears that the overall effect of the policy change has been minimal; the SEC has required and obtained admissions of guilt with settlement only seven times since this policy change.²¹¹

E. OTHER EXTERNAL INDICATORS OF BIAS

Finally, in its reaction to complaints about its enforcement program, the SEC is doing an increasingly poor job of portraying itself as an advo-

208. *Id.* at 2403 (citing *Wiener v. United States*, 357 U.S. 349, 355–56 (1958); *Humphrey's Ex'r v. United States*, 295 U.S. 602, 629 (1935)).

209. Mary Jo White, Chair, U.S. Sec. & Exch. Comm'n, Remarks at the Council of Institutional Investors Fall Conference in Chicago, IL: Deploying the Full Enforcement Arsenal (Sept. 26, 2013), available at <http://www.sec.gov/News/Speech/Detail/Speech/1370539841202>.

210. Andrew Ceresney, Co-Director, Division of Enforcement, U.S. Sec. & Exch. Comm'n, Financial Reporting and Accounting Fraud (Sept. 19, 2013), available at <http://www.sec.gov/News/Speech/Detail/Speech/1370539845772#.VMwTKWjF9zM>.

211. See Gene Cahill et al., *Fallout from the SEC's Move to Reverse 'No Admit or Deny' Policy*, 46 S.R.L.R. 1075 (2014), available at <http://www.ralaw.com/media-events.cfm?type=article&id=543>.

cate for the public's interests. After speaking defensively about the use of administrative proceedings in several speeches, the SEC spun its enforcement division statistics in its breakdown of 2013 civil actions and administrative proceedings.²¹² It excluded follow-on and delinquent filing proceedings to make its total proportion of administrative proceedings look smaller in comparison to the proportion of civil proceedings.²¹³ But when the SEC said it filed a record number of enforcement actions in 2011, it inconsistently included follow-on and delinquent filings administrative proceedings in that number.²¹⁴

This recent statistical slant goes hand-in-hand with the SEC's Internet-era habit of using press releases to sway public opinion in its favor. The SEC's website contains press releases updating the public on recently initiated enforcement actions or touting the Commission's victories in administrative or civil proceedings.²¹⁵ But as one commentator has recently noted, the SEC often fails to publicly acknowledge its court losses.²¹⁶ This approach does not promote agency transparency to the public, and it can continue to harm the accused's reputation for years because the initial press release detailing the accusations often stays near the top of search engine results. Perhaps even more concerning, the Commission's pre-hearing press releases can sometimes blur the line between informative and actively persuasive.²¹⁷ If the SEC wants to combat the perception that bias mars its in-house proceedings, it could start by addressing the way it conducts public relations.

V. A PROPOSAL TO REFORM THE SEC ADMINISTRATIVE ENFORCEMENT PROCESS

The aforementioned constitutional challenges may provide remedies to individual defendants, but the larger problems with the SEC's administrative structure would likely remain intact. The following subsections propose revisions to the SEC Rules of Practice and objective criteria for bringing administrative proceedings.

212. Andrew Ceresney, Director, Division of Enforcement, U.S. Sec. & Exch. Comm'n, Remarks to the American Bar Association's Business Law Section Fall Meeting (Nov. 21, 2014), *available at* <http://www.sec.gov/News/Speech/Detail/Speech/1370543515297#.VMnnAWjF9zM>.

213. *Id.*

214. Gallu, *supra* note 86.

215. *SEC Litigation Releases Index*, U.S. SEC. & EXCH. COMM'N, <http://www.sec.gov/litigation/litreleases.shtml> (last updated Apr. 16, 2015).

216. See Russell G. Ryan, *Mum's the Word about SEC Defeats*, WALL ST. J., June 3, 2013, at A15.

217. See Russell G. Ryan, *Get the SEC Out of the PR Business*, WALL ST. J. (Nov. 30, 2014, 5:33 PM), <http://www.wsj.com/articles/russell-g-ryan-get-the-sec-out-of-the-pr-business-1417386821> (noting some pre-hearing press releases used "colorful words and phrases like 'tricks,' 'calculated fraud,' 'reaping substantial profits,' and 'choosing profits over compliance'" to describe respondents' conduct).

A. DEVELOP OBJECTIVE CRITERIA FOR BRINGING
ADMINISTRATIVE PROCEEDINGS

The SEC Division of Enforcement released a four-page document, crafted similarly to a press release, on May 8, 2015 that outlined some of the factors it considers when it chooses a legal forum for its enforcement actions.²¹⁸ While it said that it uses “no rigid formula,” the Division of Enforcement said it considers the following factors: (1) “[t]he availability of the desired claims, legal theories, and forms of relief in each forum”; (2) “[w]hether any charged party is a registered entity or an individual associated with a registered entity”; (3) “[t]he cost-, resource-, and time-effectiveness of litigation in each forum”; and (4) “[f]air, consistent, and effective resolution of securities law issues and matters.”²¹⁹ These four factors are a good start and perhaps an impressive display of initiative by the SEC given the demand for such guidelines. However, they are not exhaustive—even the release admits that—and the Division of Enforcement should consider other factors also relevant to the administrative respondent.²²⁰

The Commission should additionally consider such factors as (1) the investigation’s length; (2) whether the claim is negligence-based or fraud-based; (3) whether expert testimony would be required to obtain a favorable verdict; (4) the amount of witnesses involved and their availability (given the administrative courts’ limited subpoena power); (5) the number of documents that the SEC expects it will review; and (6) the remedies that the SEC seeks.²²¹ Most of these criteria go to whether the complexity of the case might be better suited for federal court adjudication. One SEC commissioner has publicly advocated for such a system,²²² but at least two others have indicated that they would not be in favor of adopting any particular guidelines.²²³

The SEC recently hired an ombudsman “who will act as a liaison in resolving problems that retail investors may have with the Commission or self-regulatory organizations.”²²⁴ It would be wise for the Commission to

218. *Division of Enforcement Approach to Forum Selection in Contested Actions*, S.E.C. Division of Enforcement, available at <http://www.sec.gov/divisions/enforce/enforcement-approach-forum-selection-contested-actions.pdf>.

219. *Id.*

220. *Id.*

221. See Lieberman, *supra* note 145, at *5.

222. Michael S. Piwowar, Commissioner, U.S. Sec. & Exch. Comm’n, Remarks at the “SEC Speaks” Conference 2015: A Fair, Orderly, and Efficient SEC (Feb. 20, 2015), available at http://www.sec.gov/news/speech/022015-spchcmshp.html#.VPTLM_nF9zM (noting that “[t]o avoid the perception that the Commission is taking its tougher cases to its in-house judges, and to ensure that all are treated fairly and equally, the Commission should set out and implement guidelines for determining which cases are brought in administrative proceedings and which in federal courts”).

223. Sarah N. Lynch, *SEC Official Calls for Guidelines on When Cases are Brought In-House*, REUTERS (Feb. 20, 2015 3:03 PM), <http://www.reuters.com/article/2015/02/20/us-sec-trials-idUSKBN0LO23020150220>.

224. Press Release, U.S. Sec. & Exch. Comm’n, Tracey L. McNeil Named as SEC’s First Ombudsman (Sept. 5, 2014), available at <http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370542869949>.

ensure that the ombudsman solicited comments about the agency's administrative proceeding criteria and its Rules of Practice. She could then submit those comments to a revisions committee, which could either implement changes or propose legislation.

B. REVISE THE SEC RULES OF PRACTICE

In order to solve these larger, systemic issues, the SEC's Rules of Practice must be revised, somewhat reversing the effects of 1993 and 1995 Revisions to the SEC's Rules of Practice.²²⁵ Those revisions went into effect largely to make the Commission's internal court system speedier and more efficient.²²⁶ However, because these internal courts now exercise the same general authority as federal courts in enforcement actions against non-regulated entities, the Rules of Practice must contain protections much more similar to the ones that the Federal Rules of Civil Procedure afford. Though some commentators consider it unlikely that the SEC would voluntarily enact these revisions,²²⁷ even the SEC's general counsel recently said that it would be "reasonable" to consider revising the Rules of Practice "to make sure the process is fair" and suggested that the current rules might be out of date.²²⁸ Legislative action would be required in lieu of self-imposed changes. If these Rules of Practice changes occur, the SEC may have to bring fewer administrative enforcement actions to compensate for an inevitable slowdown in case-by-case processing time. But that slowdown is a necessary reflection of the wider range of increasingly complex securities cases that the Commission wants to bring in-house.

Generally, these revisions should help solve problems with the Rules of Practice that this Article has already explored. The three-tiered decision deadline system of 120, 200, or 300 days should be removed or should at least reflect a minimum one-year period for the proceedings to take place. Alternatively, the respondent should be able to motion for a decision deadline extension of 60 or 120 days, and the ALJ should have the authority to grant that motion. The SEC should disclose a list of fact witnesses within one month of initial service, and the ALJ should not have discretion concerning whether to allow deposition of the Commission's fact witnesses. Further, respondents should receive summary reports from SEC expert witnesses prior to trial, and they should have the ability to depose those expert witnesses.²²⁹ Finally, these proceedings should use the Federal Rules of Evidence, if not in all cases, at least in cases involving non-regulated entities.

225. Rules of Practice, Exchange Act Release No. 34-33,163, 55 S.E.C. Docket 1001 (Nov. 5, 1993).

226. See *supra* text accompanying notes 44–54.

227. See Lieberman, *supra* note 145, at *5.

228. Joel M. Cohen, *SEC Plans to Play Insider-Trading Cases on Home Court*, NAT. L.J. (Sept. 16, 2014), <http://www.nationallawjournal.com/id=1202670286446/SEC-Plans-to-Play-InsiderTrading-Cases-on-Home-Court-?slreturn=20150030091046>.

229. See Lieberman, *supra* note 145, at *5 n.26 (citing RP 360, 17 C.F.R. § 201.235).

Some proposed procedural changes could directly affect who decides the respondents' cases. As several experts have already suggested,²³⁰ the SEC could remove a perception of in-house bias by following the lead of about two dozen states, including New Jersey,²³¹ and by using independent ALJs who work from outside of the agency. Additionally, given how damaging extended litigation can be to an innocent respondent, appeals of ALJ decisions should advance immediately to Article III judges rather than to the Commission.

VI. CONCLUSION

The SEC's administrative enforcement system did not worsen overnight; its priorities changed over a series of decades and several significant pieces of legislation. Improvement will take time. However, the Due Process, Equal Protection, and Appointments Clause attacks discussed, while largely valid, only arose recently, and they are primarily a product of the Commission's increasingly improper use of its administrative proceedings. Such claims will continue for the foreseeable future unless at least one of two things occur: (1) the Supreme Court decides the validity of those claims; or (2) the SEC's Rules of Practice and criteria are revised to reflect the interests of these petitioners who believe they are being treated unfairly. Those suggested revisions align completely with the SEC's mission to serve and protect the public, and they are the best long-term solution for ensuring the stability of the Commission's administrative court system.

230. See Morgenson, *supra* note 7; see also Cohen, *supra* note 228.

231. See N.J.S.A. 52:14B-1 et seq.; see also N.J.S.A. 52:14F-1 et seq.